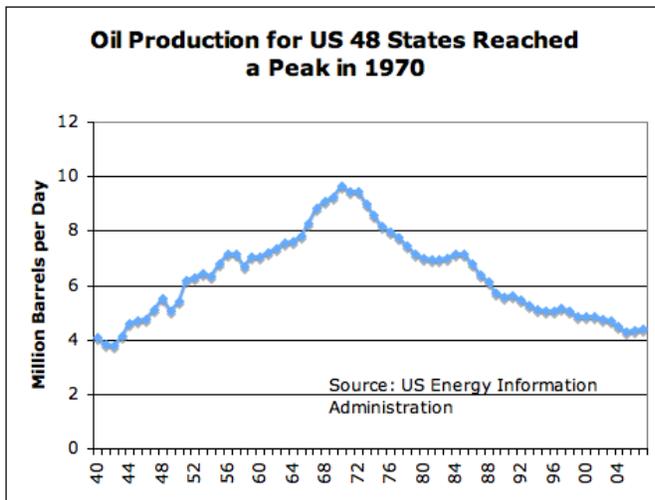




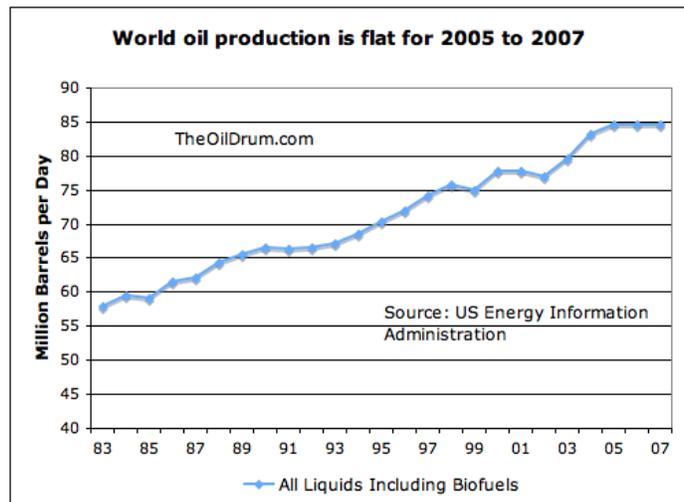
It is not hard to see that the US has some major trouble ahead for it. Politicians have been “kicking the can” for years when it comes to a real fix for social security and a credible way to reduce the unsustainable amount of debt that has been building up. These issues will surely force our country to make some tough decisions in the next 10 years as millions reach social security’s retirement age and more and more of the national debt needs to be refinanced. Unfortunately, I think we have another game changer that will be creeping into our lexicon on top of these problems—peak oil.



Peak oil is a theory developed by M. King Hubert in the 50s and 60s that says that a field, country, or the Earth will eventually reach a maximum rate of petroleum production and then forever decline. He correctly predicted that the US would reach peak oil in the 1970s. The chart to the left shows that the United States peaked in 1970 at just shy of 10 million barrels per day.<sup>1</sup> Despite new technology, and new oil field discoveries, we have never been able to get more barrels of oil per day from the ground since we hit our peak 40 years ago. Many

experts believe the *world* has already peaked or is about to peak in the next ten years (see chart below).

A senior official of the International Energy Agency recently stated "The IEA in 2005 was predicting oil supplies could rise as high as 120m barrels a day by 2030 although it was forced to reduce this gradually to 116m and then 105m last year." He added, "Many inside the organization believe that maintaining oil supplies at even 90m to 95m barrels a day would be impossible but there are fears that panic could spread on the financial markets if the figures were brought down further. And the Americans fear the end of oil



Charts courtesy of theoil drum.com

<sup>1</sup> <http://www.theoil drum.com/node/4041>

supremacy because it would threaten their power over access to oil resources.”<sup>2</sup>

Peak oil does not mean that we are going to run out of oil, it just means that the world will reach a maximum amount of oil that we can extract per day. We will get to a limited supply and there will be oil; the question will be how much are we willing to pay for it? This will be a very big issue and the world will begin to see how we have taken oil for granted all these years. Many business models that depend on cheap fuel will no longer work. What will happen when the shipping costs make it no longer profitable for raw materials to be shipped from South America to be assembled in Asia and sold in the US? How will farmers in the South survive if they are not able to ship out-of-season vegetables to the North East?

If we don't begin making major strides in research for alternative energy, the world that we have come to know could look very different in the future. Don't forget, everything that you own that is made of plastic comes from oil. There are also more than three billion hard-working people in emerging markets countries that will continue to increase their oil consumption. For the first time ever, more vehicles were sold in China in 2009 than in the US.<sup>3</sup>

There are some very good battery powered cars being developed, but their biggest limitation is how far you can drive them before they need to be recharged. And I for one, will never get on an airplane that is only powered by solar panels. We need a renewable liquid fuel and believe it or not, the answer may be liquid ammonia. You can convert your car to run on ammonia or  $\text{NH}_3$  with only minor modifications to the fuel injection system. Here is a video of Greg Vezina driving his 1981 Chevy Impala that he converted to run on ammonia:

<http://www.youtube.com/watch?v=8vwmzkn0paM&feature=Playlist&p=E9FCE9A93E178F8E&index=30>

One of the most amazing things about this video is that he actually converted his Chevy back in 1981. Ammonia was also used to fuel a fleet of motor buses in Belgium during WWII and the X-15 rocket plane in the 1960s.<sup>4</sup> The truck below was driven from Detroit to San Francisco during the



summer of 2007 using a mixture of gasoline and ammonia. Unfortunately, the US and Canada have made no real strides to make this technology a reality for our transportation. Every single president since Nixon has promised to make us “energy independent.” What have they done?

According to its website, the

[NH3car.com](http://www.nh3car.com)

<sup>2</sup> <http://www.guardian.co.uk/environment/2009/nov/09/peak-oil-international-energy-agency>

<sup>3</sup> <http://www.2ljworld.com/news/2009/dec/11/china-surpasses-us-auto-sales/>

<sup>4</sup> <http://www.ammoniafuelnetwork.org/index.html>

Department of Energy was activated on October 1, 1977 by Jimmy Carter and is responsible for “long-term, high-risk research and development of energy technology, federal power marketing, energy conservation, the nuclear weapons program...”

Whitehouse.gov states that the Department of Energy has 16,000 employees and 100,000 contractors. In 2003 the department spent \$19.8 billion.<sup>5</sup> Exactly what are those 116,000 people doing with our tax money? We are going to need several substitutes to petroleum based fuel if we want to keep a semblance of the lifestyles that we are accustomed to. Forcing us to use a 10% ethanol mixture that comes from higher priced corn when we could be importing cheaper ethanol made from Brazilian sugar cane is not going to cut it.<sup>6</sup> I believe that at least one of the substitutes needs to be a liquid fuel that will allow vehicles to refuel when making long trips. I also believe that mankind will eventually come up with alternatives. It wasn't that long ago that we were worried about forest depletion for wood to heat our homes. We then killed off too many whales for their oil. We will get transitioned to alternative energy and all of these technologies will create jobs in the United States.

Here are some of the reasons I am excited about anhydrous ammonia (compressed liquid ammonia) as a fuel that I gleaned from The Ammonia Fuel Network's website<sup>7</sup>:

- We already producing about 130 million tons of ammonia world-wide per year.
- It is carbon free and produces no green house gases on combustion
- There is already some infrastructure in place to deliver it including 3,000 miles of pipelines with a retail outlet in practically every state, 800 outlets in Iowa alone.
- Ammonia is comparable to or lower in price than gasoline on an equal energy basis.
- Building renewable ammonia infrastructure will create jobs in America.
- You can make ammonia from ocean water (we aren't going to run out of that) and air.

Most ammonia today is produced using natural gas, but it can also be made using clean, alternative energies. Imagine a wind turbine or nuclear power plant near an ocean. It can extract hydrogen from the water and nitrogen from the air and combine them into ammonia to be transported to fuel stations across the nation.

According to Matt Simmons, author of “Twilight in the Desert,” the state of Maine is planning on building around 90 deep water wind turbines that will be 70 to 90 stories tall.<sup>8</sup> He thinks that they could produce the equivalent energy of 5 nuclear power plants. You can read more about Maine's exciting project here:

<http://www.oceanenergy.org/energysystem.asp>

The only drawbacks that I see for using ammonia as a fuel is the cost of converting our current infrastructure and fighting established interests. Although we have a lot of infrastructure in place to store and transport the fuel, we don't have nearly enough to support the kind of growth this

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<sup>5</sup> <http://www.whitehouse.gov/omb/rewrite/budget/fy2004/energy.html>

<sup>6</sup> [http://www.associatedcontent.com/article/233100/ethanol\\_from\\_corn\\_vs\\_ethanol\\_from\\_sugarcane.html](http://www.associatedcontent.com/article/233100/ethanol_from_corn_vs_ethanol_from_sugarcane.html)

<sup>7</sup> <http://ammoniafuelnetwork.org/why.html>

<sup>8</sup> [http://www.youtube.com/watch?v=5feSGZN\\_Zx0](http://www.youtube.com/watch?v=5feSGZN_Zx0)

technology could have. It will also cost billions and take a very long time to convert filling station tanks to hold NH<sub>3</sub>. Let's hope ideas like this spread rapidly because one way or another, we are going to be making a change—I just hope it is on our terms.

## Markets

The S&P 500 is up 67% from its March 6, demonic 666 low. According to the Leuthold Group, the median return of all bull markets for the S&P is 83%. I continue to believe that we are in a short term bull market in the context of a longer term bear market. If history is any guide, we probably have 5-10 more tough years ahead of us. At the March low, we did not get a “once in a lifetime” buying opportunity. Stocks were cheap, but they did not get to the valuations that we saw in 1932, 1949, and 1982. I think it's more likely than not, that the S&P 500 goes a little higher from here and peaks sometime in 2010.

Markets can correct downwards or sideways. So far, this bull has had two sideways corrections as can be seen in the chart below. On December 21<sup>st</sup>, 2009, the market broke out of its trading range. It is still too early to tell if this is a genuine break out move higher or a head fake. In my view, conservative investors should be using rallies to reduce equity exposure.



Chart courtesy of [StockCharts.com](http://StockCharts.com)

I believe 2010 will be a particularly difficult year to navigate for investors. I do look forward to seeing how all this turns out. We live in some very interesting times and the imbalances that have

built up over the last 30 years will get resolved, it is just a matter of how. With that, I leave you five possible headlines for financial markets in 2010.

**Five Potential Black Swans for 2010** (These are not predictions, but events that *could* be the major headlines this year)

**1. A PIIG leaves the Euro-** Everyone has heard of the BRIC countries, but what about the PIIGS (Portugal, Ireland, Italy, Greece, and Spain)? These countries are the polar opposites of BRICs. They have enormous amounts of debt, high unemployment, and are soon going to be forced to cut their social spending as their populations age. These countries would love to print money to pay off debts and try to inflate their way out of the mess they have gotten themselves into.<sup>9</sup> Their goals are not aligned with the mandate of the European Central Bank to keep prices stable. This is the biggest test the Euro has faced since its inception. We might even see a default.

**2. Global Food Crisis begins-** Food inventories are as low as they have been in decades.<sup>10</sup> From China's Wheat Belt to Argentina, many of the world's agricultural producing countries have had very bad weather for farming. India had the weakest monsoon season since 1972.<sup>11,12</sup> "The politicians had best be able to at least feed their populations or they're going to have uprisings," said Jeff Saut, chief investment strategist of Raymond James & Associates.<sup>13</sup>

**3. U.S. and Iran go to war-** The Iran Refined Petroleum Sanctions Act was passed by the House on December 15, 2009 by a vote of 412-12. Congress is probably thinking that sanctions will impoverish the Iranians and they will in turn get angry with their leaders. I think this is the wrong way to look at it and try to put myself in the shoes of a citizen in the other country. Let's say China was to impose sanctions on the US. Are we more likely to overthrow the Obama administration because of the strife that we are feeling or would we be more likely to be angry with the Chinese? Here is what Congressman Ron Paul had to say about the bill:

Too many forget that the quagmire in Iraq began with an embargo. Sanctions are not diplomacy. They are a precursor to war and an embarrassment to a country that pays lip service to free trade. It is ironic that people who decry isolationism support actions like this.<sup>14</sup>

**4. US and Pakistan go to war-**We live in a crazy world. The Nobel Peace Prize winner has just escalated the war in Afghanistan by sending 35,000 more troops even though one of his national security advisors, James Jones, has recently estimated we are fighting 100 people. Jones said "The al-Qaida presence is very diminished," he said. "The maximum estimate is less than 100 operating in the country, no bases, no ability to launch attacks on either us or our allies."<sup>15</sup> Something doesn't add up. Why are we sending 35,000 more troops to look for "less than 100" Taliban? I am

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<sup>9</sup> [http://www.bloomberg.com/apps/news?pid=newsarchive&sid=a1R\\_ghfZ20rw](http://www.bloomberg.com/apps/news?pid=newsarchive&sid=a1R_ghfZ20rw)

<sup>10</sup> [http://eclipptv.com/viewVideo.php?video\\_id=9093](http://eclipptv.com/viewVideo.php?video_id=9093)

<sup>11</sup> <http://topics.nytimes.com/top/news/science/topics/drought/index.html>

<sup>12</sup> <http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aj2ommyY0Em4>

<sup>13</sup> <http://www.bloomberg.com/apps/news?pid=newsarchive&sid=aBYSp0.XfXZs>

<sup>14</sup> [http://www.house.gov/htbin/blog\\_inc?BLOG,tx14\\_paul,blog,999,All,Item not found,ID=091221\\_3622,TEMPLATE=postingdetail.shtml](http://www.house.gov/htbin/blog_inc?BLOG,tx14_paul,blog,999,All,Item not found,ID=091221_3622,TEMPLATE=postingdetail.shtml)

<sup>15</sup> [http://www.huffingtonpost.com/2009/10/04/jones-v-mcchrysal-obama-\\_n\\_309066.html](http://www.huffingtonpost.com/2009/10/04/jones-v-mcchrysal-obama-_n_309066.html)

concerned that we are increasingly angering the people of Pakistan by infringing on their sovereignty and accidentally murdering their civilians. It is estimated that we have bombed between 300 and 1000 people by accident. How far will we extend our pre-emptive War on Terror? Former advisor to General Petraeus, David Kilcullen, wrote “Every one of these dead non-combatants represents an alienated family, a new revenge feud, and more recruits for a militant movement.”<sup>16</sup> Let’s not forget that Pakistan is a nuclear power.

**5. The Federal Reserve gets a real audit-** When the “Patriot Act” was passed, we were told that if we had nothing to hide, we had nothing to worry about. That is the question that I pose to the Federal Reserve. I don’t know what they have been doing in the dark and behind closed doors, but it appears that they will continue to do everything in their power to fight Bloomberg’s Freedom of Information Request and HR 1207.<sup>17</sup> They have even hired a former lobbyist from Enron to try and manage its relations with Congress.<sup>18</sup> You can’t make this stuff up! I think if we get a true audit, we could find a major skeleton in their closet. Many congressmen are waking up to the fact that the Fed has an enormous amount of power and very little transparency and oversight. If you haven’t seen Congressman, Alan Grayson’s questioning of the General Counsel for the Fed, please watch it here:

<http://www.youtube.com/watch?v=mXmNpdYpfnk>

Have a Happy New Year and Hook ‘em Horns on the 7<sup>th</sup>!

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<sup>16</sup> <http://www.newyorker.com/online/blogs/newsdesk/2009/10/jane-mayer-predators-drones-pakistan.html>

<sup>17</sup> <http://www.bloomberg.com/apps/news?pid=newsarchive&sid=akxLAK7L1S8A>

<sup>18</sup> <http://www.bloomberg.com/apps/news?pid=20601103&sid=aZjQKyLci1AM&refer=us>